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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of	)	
	)	
Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area	)	CC Docket No. 96-149
	)	
and	)	
	)	
Policy and Rules Concerning the Interstate, Interexchange Marketplace	)	CC Docket No. 96-61

OPPOSITION OF MCI TELECOMMUNICATIONS CORPORATION TO PETITIONS FOR RECONSIDERATION

MCI TELECOMMUNICATIONS CORPORATION

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Dated: September 8, 1997

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SUMMARY

MCI opposes the petitions filed by Anchorage Telephone Utility, the National Telephone Corporative Association (NTCA), ALLTEL Communications, Inc. and the United States Telephone Association (USTA) to reconsider the Second Report and Order in CC Docket No. 96-149 and Third Report and Order in CC Docket No. 96-61 (Order) and to eliminate or modify the Competitive Carrier separate affiliate requirements imposed by the Order on ILEC provision of in-region interstate, interexchange services.

USTA and Anchorage argue that since Congress decided not to include ILECs within the coverage of the separation requirements of Section 272, the Commission should not impose any type of separation requirements on them. There is nothing in the language of the 1996 Act, however, or in any legislative history, that suggests such a conclusion. Moreover, as the Order points out, Section 601(c)(1) states that the Commission should not presume that Congress intended to supersede any of its regulations unless expressly so provided.

The alternative safeguards -- including the joint cost allocation rules -- that have been implemented and the interexchange competition that has developed since the Competitive Carrier separation rules were first established do not diminish the need for those rules. Since most ILECs providing interexchange services are still subject to rate-of-return regulation, they still have a powerful incentive and the ability to misallocate costs. Also, the Part 64 rules have not been very effective, as shown by the brazen cost misallocations and cross subsidies reported in recent federal and state audits. The current vigor of interexchange competition also does not lessen the need for

the separation rules, since they were imposed in order to curb the leveraging of the ILECs' local bottleneck power, which remains virtually undiminished.

The petitioners argue that since they are resellers of the IXCs' interexchange services, they are in no position to discriminate against IXCs, to misallocate costs or to carry out a price squeeze against IXCs. It is not true, however, that most ILECs providing in-region interexchange services are pure resellers of such services. Instead, most such ILECs provide the access portion of their in-region interexchange services, providing tremendous opportunities for cost shifting through failure to properly impute access costs in their interexchange rates. Moreover, even an ILEC that is a pure reseller of interexchange services could impose a price squeeze on other IXCs, since the IXCs could not pass on inflated access charges to their retail customers. The ILECs would still be able to subsidize their interexchange services with their excessive access revenues, resulting in lower ILEC interexchange rates than IXCs could afford to charge, given their excessive access costs. The inclusion of the ILECs' excessive access charges in the wholesale rates charged back to the ILECs by the IXCs would only result in an internal transfer for the ILECs -- from their interexchange operations to their access operations -- rather than a true cost.

The ILECs also argue that the price squeeze argument depends on the unrealistic assumption that they can raise access charges at will. As rate-of-return regulated carriers, however, they can raise access rates through cost misallocations. Moreover, their access rates are already grossly excessive, allowing them to impose price squeezes now.

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OPPOSITION OF MCI TELECOMMUNICATIONS CORPORATION
TO PETITIONS FOR RECONSIDERATION

MCI Telecommunications Corporation (MCI), by its undersigned attorneys, hereby opposes the petitions filed by Anchorage Telephone Utility (Anchorage), the National Telephone Cooperative Association (NTCA), ALLTEL Communications, Inc. (ALLTEL) and the United States Telephone Association (USTA) for reconsideration of the Second Report and Order in CC Docket No. 96-149 and Third Report and Order in CC Docket No. 96-61 (Order) released in the above-captioned proceedings on April 18, 1997.[1] These four petitioning independent local exchange carriers (LECs) and LEC trade associations seek the elimination or various modifications of the requirement in the Order that incumbent LECs (ILECs) be subject to the Commission's Competitive Carrier separation rules[2]

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[1] FCC 97-142 (released April 18, 1997).

[2] Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Therefor, CC Docket No. 79-252, Notice of Inquiry and Proposed Rulemaking (Notice), 77 FCC 2d 308 (1979); First Report and Order (First Report), 85 FCC 2d 1 (1980); Further Notice of Proposed Rulemaking, 84 FCC 2d 445

in their provision of in-region interstate, interexchange services. For the reasons set forth below, the ILEC petitions should be denied.

Background

In the Order, the Commission found that although ILECs would not be able to exercise sufficient market power in in-region interexchange services to raise prices by restricting output, they do have the ability and incentive to use their bottleneck facilities to engage in anticompetitive conduct. Their monopoly power enables them to misallocate costs from their in-region, interstate, interexchange services to their monopoly local exchange and access services, to discriminate against other interexchange carriers (IXCs) with respect to the provision of exchange and exchange access services and to initiate price squeezes against other IXCs through excessive access charges.

Accordingly, the Commission required that independent ILECs provide their in-region, interstate, interexchange services through affiliates that satisfy the Competitive Carrier

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(1981); Second Further Notice of Proposed Rulemaking, 47 Fed. Reg. 17308 (1982); Second Report and Order (Second Report), 91 FCC 2d 59 (1982), recon. denied, 93 FCC 2d 54 (1983); Third Report and Order (Third Report), 48 Fed. Reg. 46791 (1983); Fourth Report and Order (Fourth Report), 95 FCC 2d 554 (1983), vacated, AT&T v. FCC, 978 F.2d 727 (D.C. Cir. 1992), cert. denied, MCI Telecommunications Corp. v. AT&T, 113 S. Ct. 3020 (1993); Fourth Further Notice of Proposed Rulemaking, 96 FCC 2d 1191 (1984); Fifth Report and Order (Fifth Report), 98 FCC 2d 1191 (1984); Sixth Report and Order (Sixth Report), 99 FCC 2d 1020 (1985), vacated sub nom., MCI Telecommunications Corp. v FCC, 765 F.2d 1186 (D.C. Cir. 1985).

separation requirements. The Commission determined that those requirements -- that the affiliate maintain separate books of account, not jointly own transmission or switching facilities with the LEC and acquire any services from the LEC at tariffed rates, terms and conditions or on the same basis as requesting carriers that have negotiated interconnection agreements under Section 251 of the Communications Act -- aid in the prevention and detection of such anticompetitive conduct and are not unreasonably burdensome in light of their benefits. The Commission also determined that it should not exempt any ILECs from those requirements on the basis of size or rural service territory, since those factors do not affect an ILEC's bottleneck power within its service region and thus its ability and incentive to engage in anticompetitive behavior in connection with its in-region interexchange services.[3]

The ILECs' Petitions

For the most part, the petitioners elaborate on contentions that have already been fully addressed in the Order and thus need not be exhaustively reviewed again. USTA and Anchorage request that the separation requirements be eliminated for all ILEC in-region interexchange services, arguing that the Part 64 joint cost allocation rules and other safeguards offer more than adequate protection against the anticompetitive conduct that is the target of the separation requirements, especially for ILECs

[3] Order at ¶¶ 156-83.

that resell the interexchange services of other IXCs. They and ALLTEL also request that a "sunset" provision along the lines of the sunset provision in Section 272(f)(1) of the Act be incorporated into the separation requirements, so that ILECs do not remain subject to such requirements after the separation requirements in Section 272 of the Act have been lifted from the Bell Operating Companies (BOCs).

Anchorage also requests that the Commission add a procedure by which an ILEC could seek a waiver of the separation requirements when local competition develops in its territory. NTCA requests elimination of the requirement that the in-region interexchange affiliate be a separate legal entity. Finally, ALLTEL requests that the separation requirements be eliminated for ILECs serving less than two percent of the nation's access lines, raising most of the same arguments as USTA and Anchorage.

ARGUMENT

A. Nothing in the Telecommunications Act of 1996 Suggests or Implies That the Commission Should Not Impose Any Separation Requirements on ILEC Provision of Interexchange Services

USTA and Anchorage repeat the oft-rejected claim that since Congress decided, in drafting Section 272 of the Act -- the separate affiliate provision applicable to BOC interLATA services -- not to impose a separation requirement on non-BOC ILEC provision of interexchange services, the Commission should not do so. They cite no legislative history, however, supporting the view that Congress had any intention whatsoever as to non-BOC

ILEC provision of interexchange services. An after-the-fact letter from a few members of Congress, cited by USTA and Anchorage, hardly qualifies as even the weakest form of legislative history. Moreover, as the Commission found in the Order, Section 601(c)(1) of the Telecommunications Act of 1996 (1996 Act) provides that the Commission is not to presume that Congress intended to supersede any of its regulations unless expressly so provided.[4] The afterthought reflected in the Congressional letter cited by USTA and Anchorage cannot change the explicit instruction in Section 601 that the 1996 Act has, in the words of the heading of Section 601(c)(1), "no implied effect" on any other Commission policies.

To drive the point home, Congress stated in the sunsetting provision of the separate affiliate section of the 1996 Act that USTA cites -- Section 272 of the Communications Act -- that "[n]othing in this subsection shall be construed to limit the authority of the Commission under any other section of this Act to prescribe safeguards consistent with the public interest, convenience and necessity."[5] Clearly, if the sunsetting of the separate affiliate provision cannot be construed to limit the Commission's authority to prescribe any safeguards it deems appropriate, the scope of the separate affiliate provision itself cannot be so construed. Thus, contrary to the LECs' implied intent argument, Congress made no decision in Section 272, or

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[4] Order at ¶ 168 & n. 480.

[5] Section 272(f)(3) of the Act.

anywhere else in the 1996 Act, to preclude the Commission's imposition of a separate affiliate requirement on ILEC provision of in-region interexchange services or any other "safeguard" it deems necessary in the public interest.

B. The Part 64 Rules and Other Safeguards and the Development of Interexchange Competition Since the Promulgation of the Competitive Carrier Separation Rules Do Not Diminish the Need for Such Separation

The four ILECs mentioned above argue that a separate affiliate requirement is not necessary because of the implementation of alternative safeguards and the development of interexchange competition since the Competitive Carrier separation rules were first established. In particular, USTA, Anchorage and ALLTEL dwell on the Part 64 rules as protection against cost misallocation equivalent to that achieved through the separate affiliate rules. Cost misallocation, however, is especially problematical for ILECs providing interexchange services, since almost all of them provide their access services under rate-of-return regulation.[6] As the LECs have argued for years, and the Commission has repeatedly found, rate-of-return regulation generates much greater incentives to misallocate costs than price cap regulation, since, under the former, the shifting of costs from competitive services to monopoly services can be used to justify increased monopoly rates.[7] Thus, in terms of

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[6] See USTA Pet. at 10.

[7] See, e.g., Order at ¶ 106 (price cap regulation reduces incentives to misallocate costs because it "`severs the direct

cross subsidy incentives, most non-BOC ILECs providing interexchange services are in the same situation today that all BOCs and ILECs were when the Competitive Carrier separation rules were first established in 1984 -- long before the advent of price cap regulation.

Moreover, the Part 64 rules have not worked well. As explained in Attachment A, recent audits carried out by state and federal authorities demonstrate widespread cost misallocations and cross-subsidies by the BOCs and GTE, especially under rate-of-return regulation.[8] Even more recently, NECA audits uncovered "numerous apparent violations of the Commission's [accounting] rules committed by" the BOCs in connection with their reported adjustments to the common line revenue pool for 1988 and the first quarter of 1989.[9]

Furthermore, the cost allocation and other accounting rules are only as good as the Commission's willingness and ability to enforce them with sufficient penalties to inhibit future violations. That final link in the chain may be the weakest of all. In 1995, as explained in Attachment A, the Commission released a summary of its audit of the BOCs' accounting for lobbying costs, which found $116.5 million in misclassified

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link between regulated costs and prices'").

[8] Comments of MCI Telecommunications Corporation at 12-15, Bell Operating Company Provision of Out-of-Region Interstate, Interexchange Services, CC Docket No. 96-21 (March 13, 1996).

[9] See, e.g., Consent Decree Order, The BellSouth Telephone Operating Companies, AAD No. 93-148, FCC 96-412 (released Nov. 1, 1996).

lobbying costs during the period from 1988 through 1991.[10] Moreover, the inflated access rates resulting from such misallocations were carried over into the BOCs' access rates under price cap regulation. In spite of these egregious violations, the Commission merely required the BOCs to reduce their price cap indices to correct the problem on a going-forward basis and failed to take any remedial action for the past ratepayer injuries resulting from these misallocations.[11] The Commission's failure to take such remedial action confirms the inadequacy of the entire cost accounting regulation and audit function, since the ILECs apparently have a "free shot" at any accounting violation they may wish to commit, knowing that the worst that can happen is that someday, if they are caught, they might have to correct such practices only on a going-forward basis.

The cost misallocations, excessive costs and cross-subsidies uncovered by these audits, and the Commission's limp response thereto, thus demonstrate the ineffectiveness of the cost allocation regulations in preventing ILEC cross-subsidies between regulated and unregulated services. Since ILEC monopoly and regulated competitive services -- such as interexchange services -- are more similar to one another than ILEC regulated and unregulated services, allocations of costs between monopoly and

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[10] Commission Releases Summary of Lobbying Costs Audit Findings, Report No. CC 95-65 (released Oct. 26, 1995).

[11] See id.

competitive regulated services will be even more difficult to audit. Thus, the cost allocation rules, having failed at their primary mission, cannot possibly be relied upon to prevent cross-subsidies and cost misallocations between ILEC monopoly and regulated competitve services. Given the ineffectiveness of the Part 64 rules and their enforcement, the Commission cannot rely solely on those rules to prevent cost misallocations by ILECs providing in-region interexchange services. The Commission was therefore correct to supplement those rules by imposing the Competitive Carrier separate affiliate rules in this situation.

The development of vigorous interexchange competition since the Competitive Carrier separation rules were first established also does not diminish in any way the need for such separation. Originally, the need for separation between the ILECs' local exchange and interexchange services did not emanate from the then-nascent state of competition in interexchange services, but, rather, from the ILECs' bottleneck control of local exchange facilities. Since that control has not appreciably diminished since the Competitive Carrier separation requirements were first promulgated, those requirements are still just as necessary for ILEC in-region interexchange services.

C. The ILECs' Resale of Interexchange Services Does Not Undercut the Rationale for the Separation Requirements

USTA, NTCA and ALLTEL place their greatest emphasis on the argument that ILECs providing interexchange services are primarily resellers of the IXCs' services and thus are not in a position to discriminate against IXCs or to misallocate costs. They also argue that, for the same reason, they are not in a position to impose a price squeeze on other IXCs, since those IXCs can simply pass their costs back to the ILECs' interexchange operations in the wholesale rates they charge the ILECs.

There are several problems with these arguments. First, it is not the case that the ILECs are pure resellers of interexchange services within their own service regions. It would not make much sense for an ILEC to purchase an end-to-end interexchange service for resale within its own region, since the end user customer of the interexchange service more than likely will also be the ILEC's local exchange service customer. Thus, the ILEC will already be providing access to that customer and would have no reason to pay for the very same access service as part of the IXC's end-to-end service. Instead, in MCI's experience, the ILEC typically uses its own access services within its local service region and purchases only the interexchange portion of the end-to-end service from the IXC. None of the petitioners explains why an ILEC would pay an IXC for access service, as part of an end-to-end interexchange service, that the ILEC itself is already providing, at least on the originating end.

Since ILECs typically only purchase interexchange transport, rather than the entire end-to-end service, for resale within their service regions, they still have the ability and incentive to misallocate costs and to discriminate. They essentially provide their own access services as part of their interexchange services, generating enormous opportunities to misallocate costs through failure to properly impute the entire cost of access in their interexchange rates. ILECs are also able to shift costs and discriminate in favor of their own interexchange services by having the local exchange and access operations perform functions for the interexchange operations that are not fully reimbursed, such as by having local operators market the ILEC's interexchange services. Such a conferring of benefits derived from the ILEC's monopoly operations on its interexchange services without adequate compensation unfairly subsidizes those services, resulting in unreasonable discrimination against other IXCs, which must purchase the same inputs at inflated rates. Such monopoly benefits can be conferred on the ILEC's interexchange services whether or not the ILEC is a reseller of such services.

D. None of the Factors Cited by the ILECs, Including Their Resale of Interexchange Services, Lessens Their Ability to Inflict a Price Squeeze on Other IXCs

Moreover, even if the ILECs were pure resellers of IXC end-to-end interexchange services, they still could impose a price squeeze on other IXCs. The ILECs' purchase of IXC services for resale would not "wash out" the effects of excessive ILEC access charges, as the petitioners suggest. The IXCs would still be in the position of paying excessive access charges to the ILECs, which the IXCs would have to pass along in order to stay in business. The ILECs, however, would be able to undersell the

IXCs, using their excessive access revenues to fund their predatory interexchange rates. The inclusion of the ILECs' excessive access charges in the IXCs' wholesale rates charged back to the ILECs would not lessen the ILECs' ability to engage in a price squeeze, since the ILECs would not have to cover all of their costs in their interexchange rates. The ILECs' payment to the IXCs of wholesale rates reflecting the ILECs' own access charges only amounts to the equivalent of an internal transfer for the ILECs -- from their interexchange operations to their access operations -- rather than a real cost for the ILECs.

Thus, even if the ILECs were pure resellers of interexchange services within their own regions, they could still engage in a price squeeze in the retail market. The petitioners' argument only demonstrates that the IXCs could pass their excessive access costs along in selling their wholesale end-to-end services to the ILECs, but it ignores entirely that the IXCs could not pass those same costs along in selling to end users, who could always get a better, subsidized retail price from the ILECs. Finally, in the more likely situation, where an ILEC purchases only interexchange transmission from the IXCs for in-region resale, the risk of price squeezes is even more obvious, since the IXC cannot pass any of its excessive access costs back to the ILEC.

The petitioners also argue that the price squeeze argument depends on the ILECs being able to raise access rates at will, which, they claim, is unrealistic. Since almost all of the ILECs that provide interexchange services are subject to rate-of-return regulation, however, they retain the ability and incentive to shift costs to their access services, all of which can be recovered through higher access charges. Moreover, as MCI explained in its comments in this proceeding, BOC and ILEC access rates are already grossly excessive.[12] The Commission's access charge reductions following release of the Order hardly make a dent in the overall excessiveness of access rates. Indeed, the Commission admitted in its Access Charge Reform Order[13] that it was eliminating only "some of the distortions" that prevent access charges from "reflect[ing] the true cost of service" and that its reductions "represent [only] the first step toward ... moving such charges toward economically efficient levels."[14] The Commission went so far as to concede that a further reduction of access charges to competitive levels "would require dramatic cuts in access charges for some carriers," resulting in "a substantial decrease in revenue for incumbent LECS."[15]

Thus, the ILECs' access charges are still grossly excessive, allowing them to impose a price squeeze on IXCs immediately. Nothing more has to be done to raise rivals' access costs to an

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[12] See Hatfield Associates, The Cost of Basic Network Elements: Theory, Modeling and Policy Implications (March 1996), attached to ex parte letter from Frank W. Krogh, MCI, to William F. Caton, Secretary, FCC, Policy and Rules Concerning the Interstate, Interexchange Marketplace, CC Docket No. 96-61 (filed May 31, 1996).

[13] Access Charge Reform, et al., CC Docket No. 96-262, et al. 62 Fed Reg 31868 (June 11, 1997).

[14] Id. at 31875.

[15] Id. at 31876.

unreasonable level. Moreover, this tactic can be implemented just as effectively by an ILEC's failing to pass along reductions in the cost of providing access as by raising access rates. The ILECs are thus already in a position to inflict significant harm on interexchange competition by forcing excessive costs on the IXCs.

USTA also argues that the availability of unbundled network elements (UNEs) provides a way to bypass allegedly excessive access charges, thereby avoiding any threat of a price squeeze. The pricing of UNEs is also a difficult issue, however, and the vacating of the Commission's UNE pricing rules by the Eighth Circuit makes the determination of such pricing much more complex.[16] Thus, UNEs cannot necessarily be relied upon to offer a useful alternative to access services for the foreseeable future. Accordingly, the petitioners' arguments do not in any way diminish or undercut the Commission's stated concerns over price squeezes and the need for separation requirements to help minimize and detect such tactics.

E. ILECs Serving Less Than Two Percent of the Nation's Access Lines Are Capable of Inflicting Anticompetitive Injury and Have Done So

USTA and other petitioning ILECs also claim that there has been no evidence of harm to the interexchange market caused by non-BOC ILECs and thus there is no need for the additional

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[16] See Iowa Utilities Board v. FCC, et al., Nos. 96-3321, et al. (8^{th} Cir. July 18, 1997).

protection of separation requirements. To the contrary, MCI has been subjected to a barrage of anticompetitive assaults by the Southern New England Telephone Company (SNET), to pick one ILEC involved in the provision of interexchange service. The Order notes one informal complaint filed by MCI, which alleged that SNET was promoting its "PIC-freeze" program in order to lock out competitive IXCs.[17] SNET's conduct demonstrates that it is the possession of local bottleneck power, which ILECs enjoy to the same extent as the BOCs, that provides the ability and incentive to engage in anticompetitive conduct harmful to the interexchange market. The smaller size and scope of ILEC operations makes little difference.

ALLTEL takes the smallness argument a step further and argues for elimination of the separation requirements for those ILECs serving less than two percent of the nation's access lines. It asserts that many such ILECs cover no more than one LATA and thus have no interexchange facilities, requiring them to operate as resellers of interexchange services. There is hardly anything magical about the two percent criterion, however. SNET, for example, serves only about 1.3 percent of the nation's access lines,[18] but it has significant interexchange operations and

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[17] Letter from Donald J. Elardo, MCI, to John Muleta, Chief, Enforcement Division, Common Carrier Bureau, dated July 24, 1996, Informal Complaint No. IC96-09734, cited in Order at ¶ 172 n. 500.

[18] Petition of Southern New England Telephone Corporation for Declaratory Ruling at 26 & n. 63, Petition Requesting That Any Interstate Non-Access Service Provided by Southern New England Telecommunications Corporation Be Subject to Non-Dominant

engages in substantial anticompetitive activities. Moreover, the absence of interexchange facilities, as explained above, hardly guarantees that ILEC resellers of interexchange services cannot or will not discriminate, misallocate costs or engage in price squeezes. ALLTEL's proposed elimination of the separation requirements for ILECs serving less than two percent of the nation's access lines therefore must be rejected.

F. The Order Properly Interprets the Competitive Carrier Separation Rules to Require That the Interexchange Affiliate be a Separate Legal Entity

NTCA and other petitioners also claim that the Commission stiffened the Competitive Carrier separation requirements without notice by requiring in the Order, for the first time, that the interexchange affiliate be a separate legal entity, rather than simply a separate division of the ILEC. NTCA argues that ILECs have been operating their interexchange services as separate divisions with no discernable harm to the interexchange market and that all of the other separation requirements can be applied just as well to separate divisions as to separate legal entities. It points out that since most ILECs do not own interexchange facilities, the prohibition against joint ownership of facilities is moot in most cases.[19]

It is clear, however, that Competitive Carrier always required that the ILEC's interexchange affiliate be a separate

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Carrier Regulation, Jan. 17, 1996.

[19] NTCA Pet. at 3-5.

legal entity from the local exchange entity. Otherwise, the prohibition against joint ownership of facilities would be meaningless. NTCA never addresses this obvious flaw in its assumption about the original Competitive Carrier separation requirements. If a particular ILEC has no interexchange facilities, as NTCA suggests, the joint ownership prohibition may be irrelevant to it, but the other separation requirements should still be applied. For example, accounting separation is more effective where legal separation is also required, since it makes joint and shared costs, and the allocation thereof, more visible. There is therefore no justification for eliminating the requirement that the ILEC interexchange affiliate be a separate legal entity.

G. There is No Need for a Formal Sunset Provision in the Commission's Separate Affiliate Rules

USTA, Anchorage and ALLTEL request that the separation rules contain a formal sunset provision that would operate automatically three years after the Order became effective, and Anchorage requests the addition of a formal waiver procedure that an ILEC could use to get out from under the separation requirements if it could demonstrate that local competition had developed in its region. The petitioners argue that without such a sunset provision, ILECs could still be subject to separation requirements after the Section 272 separation requirements sunset for the BOCs.

There would be little point to such a formal sunset or waiver provision, however. The Commission announced in the Order that it will commence a proceeding in three years -- which would be mid-April 2000 -- to determine whether to lift the separation requirements for ILECs.[20] The three-year sunset provision in Section 272(f)(1), meanwhile, is geared to a BOC's authorization to provide in-region interLATA service. Since no BOC is close to obtaining such authority, the first sunset date for any BOC separate affiliate cannot occur much before the end of 2000, assuming the Commission does not exercise its authority under Section 272(f)(3) to extend the Section 272 separation requirements for that BOC. The first possible sunset for any BOC separate affiliate thus could not occur until several months after the Commission begins its proceeding to re-examine the separate affiliate requirement for the ILECs. The petitioners' concerns thus are too hypothetical to merit serious consideration of a formal sunset provision for ILEC separate affiliates. In any event, the Commission is essentially in control of both sunset dates and thus can be expected to ensure the appropriate regulatory relationship between BOCs and ILECs.

Similarly, any ILEC that believes that it can make a case for early termination of the separate affiliate requirement as applied to its provision of in-region interexchange services, for any reason, can seek a waiver of that requirement under the existing waiver procedure in Section 1.3 of the Commission's Rules. There is no reason to add another more specialized waiver

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[20] Order at ¶ 196.

procedure just for ILECs that want to demonstrate that local service competition has developed sufficiently in their regions to justify elimination of the separate affiliate requirement.

Conclusion

WHEREFORE, the USTA, Anchorage, NTCA and ALLTEL petitions for reconsideration of the Order should be denied for the reasons stated above.

Respectfully submitted,

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Dated: September 8, 1997

ATTACHMENT A

need for BOC separate interexchange affiliates under the new Section 272 of the Communications Act in any event; at that time, the Commission could take into account the BOCs' out-of-region services as part of its review.[19] For the interim period contemplated by the Notice,[20] however, separate affiliates for out-of-region interexchange services are still necessary.

The need for separate affiliates for BOC out-of-region interexchange services -- indeed, for all BOC competitive services -- is underscored by the recent critical audits of BOC and LEC affiliate transactions conducted by state and federal authorities. For example, in April 1994, the Commission and the GTE Telephone Companies (GTOCs) entered into a Consent Decree settling issues arising out of an audit of the transactions between the GTOCs and two of their nonregulated affiliates. The audit revealed that the nonregulated affiliates achieved excessive rates of return in their sales of services to the GTOCs and that the resulting excessive costs to the GTOCs were passed on to ratepayers. The terms of the Consent Decree required the GTOCs to file rate reductions, make a contribution to the United

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[19] See the new Section 272 of the Communications Act, added by Section 151 of the 1996 Act, requiring that various BOC competitive services, including in-region interexchange services, be provided through separate affiliates, and especially Section 272(f)(1), terminating the separate affiliate requirement after three years unless the Commission extends it.

[20] Notice at ¶11.